1941

American Investment Corporation v. The State Tax Commission of Utah and Irwin Arnovitz, R. E. Hammond, H. P. Leatham and B. H. Robinson : Brief of Plaintiff

Utah Supreme Court

Garfield O. Anderson; Grant A. Brown; Attorneys for Petitioners;

6312

IN THE

SUPREME COURT

OF THE STATE OF UTAH

AMERICAN INVESTMENT CORPORATION, a corporation,
Plaintiff,

vs.

THE STATE TAX COMMISSION OF UTAH and IRWIN ARNOVITZ, R. E. HAMMOND, H. P. LEATHAM and B. H. ROBINSON, the Members of said Commission,
Defendants.

No. 6312

PETITION FOR REHEARING AND BRIEF IN SUPPORT THEREOF

GARFIELD O. ANDERSON
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STATE TAX COMMISSION OF UTAH, and IRWIN ARNOVITZ, R. E. HAMMOND, H. P. LEATHAM and B. H. ROBINSON, the members of said Commission,
Defendants.
No. 6305

PLAINTIFF'S BRIEF

STATEMENT OF THE CASE

This is an original proceeding in this Court for the purpose of reveiwing a decision of the State Tax Commission of Utah, dated September 11, 1940, in the proceeding designated by the said Commission as "In the Matter of the Redetermination of Corporation Franchise Tax of AMERICAN INVESTMENT CORPORATION for the year 1937", and by which said decision the said Commission decided that there was due from plaintiff the sum of $296.37, with interest, as the unpaid deficiency on its corporation franchise tax for the calendar year 1937.

STATEMENT OF THE FACTS

American Investment Corporation, plaintiff herein, is and was at all times since October 31, 1929, a corporation organized under and by virtue of the laws of the State of Nevada, and with its principal place of business at Ely, Nevada. It is, and was at all times since March 16, 1934, qualified to do business within the State of Utah as a foreign corporation. During the year 1937 (which is the year we were concerned with) plaintiff was duly qualified to do business within the State of Idaho as a foreign corporation. It is, and was at all times since its incorporation, primarily engaged in acquiring by stock ownership the control of banking corporations, and holding the stocks thereof for the purpose of controlling the management of the affairs of such other corporations. During the calendar year it owned stock in, and exercised control of, Idaho Bank and Trust Co., a banking corporation of the State of Idaho, and Commercial Security Bank, a banking corporation of the State of .Utah During the year 1937 the said Idaho Bank and Trust Co. did no business within the State of Utah, nor has it ever done business with said state nor has it ever made or been required to make reports to the State of Utah or any departments thereof pursuant to the laws of said state or otherwise. Commercial Security Bank has at all times filed corporation franchise returns with the defendant State Tax Commission of Utah, including such return for the year 1937, and has at all times paid all taxes due from it to the State of Utah for the privilege of doing business within said state.

During the calendar year 1937 plaintiff had the following gross income:

Capital gain from sale of Ohio Oil Company Stock	$ 299.40
Capital gain from sale of Socony Vacuum Oil Co. Inc. Stock	4,424.30
Dividends on Socony Vacuum Oil Co. Inc. Stock	125.00
Dividend on Ohio Oil Company Stock	200.00
Dividends on Idaho Bank and Trust Co. Stock Stock	6,016.60
Liquidating dividend on Commercial Security Bank	112.00
Making a total gross income of	$11,177.30

All of said income was shown on plaintiff's franchise tax return but in arriving at the amount of its taxable net income plaintiff deducted from said gross income the whole thereof, except the liquidating dividend on Commercial Security Bank in the sum of $112.00. Upon the subsequent audit of said return by the Commission, the Commission on September 11, 1939, restored to plaintiff's net taxable income the entire gross income shown in plaintiff's said return and hereinabove set out, less only the following deductions:

Liquidating dividend on Commercial Security Bank	$ 112.00
Federal Tax paid to the United States on 1936 income	362.28
Other expenses	490.00

leaving, according to the Commission, a taxable net income of $10,212.47, or an increase of $10,100.47 over the amount of taxable net income as shown by plaintiff, and assessed an additional tax against plaintiff in the sum of $296.37, with interest from August 1, 1938, at the rate of 6% per annum.

Within the time allowed by law, on November 3, 1939, plaintiff duly filed its petition with the said Commission for a redetermination of said deficiency. Upon the hearing befor the Commission on said petition, the following facts were established:

That during the period in question, plaintiff was a foreign corporation, with its principal place of business at Ely, Nevada; that it was qualified to do and doing business within the State of Utah; that its primary business was in holding the stock of banking corporations for the purpose of controlling the management of the affairs thereof; that it did hold stock in and control the affairs of Idaho Bank and Trust Co., an Idaho corporation, doing no business within the State of Utah, and Commercial Security Bank, a Utah corporation; that it also owned stock in Socony Vacuum Oil Company, a corporation of the State of New York, with its principal place of business at New York City, and Ohio Oil Company, a corporation of the State of Ohio, with is principal place of business at Findlay, Ohio, which said two companies plaintiff did not control; that of its gross income during the calendar year 1937, $299.40 was a capital gain from the sale of Ohio Oil Company stock, $4,424.30 was a capital gain from the sale of Socony-Vacuum Oil Company stock, $200.00 was a dividend on the Ohio Oil Company stock, $125.00 was a dividend on the Socony Vacuum Oil Company stock, $6,-016.60 was a dividend on Idaho Bank and Trust Company stock, and $112.00 was a liquidating dividend on Commercial Security Bank stock.

Under date of September 11, 1940, the Commission rendered its decision in writing upon plaintiff's said petition

for redetermination of said deficiency, giving plaintiff notice of said decision on September 19, 1940. By said decision the Commission decided that the whole of plaintiff's gross income, less only the following deductions:

Liquidating dividend on Commercial Security Bank	$ 112.00
Federal Tax paid to the United States on 1936 income	362.28
Other expenses	490.00

constituted plaintiff's taxable net income, and assessed a deficiency tax against plaintiff in the sum of $296.37, with interest at 6 per cent per annum from August 1, 1938, to the date of the decision, and 1 per cent per month from that date until paid.

Thereafter and within the time allowed by law, plaintiff, pursuant to the provisions of Section 47, Chapter 13, Title 80, Revised Statutes of Utah, 1933, petitioned this Court to review the said decision of the Commission. Under the provisions of the Franchise Tax Act (Chapter 13, Title 80, Revised Statutes of Utah, 1933), this Court by Certiorari may review the decision of the Commission on both the law and the facts.

STATEMENT OF ERRORS

It is the contention of the plaintiff that the decision of the Commission whereby it assessed a deficiency tax against plaintiff in the sum of $296.37, with interest, is without and in excess of its powers, and unlawful, for the following reasons:

(a) That said deficiency was assessed against plaintiff pursuant to the provisions of Chapter 13, Title 80, Revised Statutes of Utah, 1933, and plaintiff is exempt from the provisions thereof by virtue of Section 5 (16) of said Chapter and Title.

(b) That said deficiency is based upon the inclusion by the Commission in plaintiff's net taxable income of the sum of $6.016.60, which sum was received by plaintiff during 1937 as dividends on stock owned by it in said Idaho Bank and Trust Company and was not derived from business done by plaintiff within the State of Utah, nor is such income assignable to business done by plaintiff within the State of Utah.

(c) That said deficiency is based upon the inclusion in plaintiff's net taxable income of the sum of $4,424.30, which sum was received by plaintiff as a gain to it from the sale of stock of Socony Vacuum Oil Company and was not derived by plaintiff from business done by it within the State of Utah, nor is it assignable to business done within the State of Utah.

(d) That said deficiency is based upon the inclusion in plaintiff's net taxable income of the sum of $125.00, which amount was received by plaintiff as dividends paid to it on stock of Socony Vacuum Oil Company and was not derived by plaintiff from business done by it within the State of Utah, nor is it assignable to business done by plaintiff within the State of Utah.

(e) That said deficiency is based upon the inclusion in plaintiff's net taxable income of the sum of $299.40, which

amount was received by plaintiff as a gain upon the sale of stock of Ohio Oil Company and was not derived from business done by plaintiff within the State of Utah, nor is it assignable to business done by plaintiff within the State of Utah.

(f) That said deficiency is based upon the inclusion in plaintiff's net taxable income of the sum of $200.00, which sum was received by plaintiff as dividends on stock of Ohio Oil Company and was not derived from business done by plaintiff within the State of Utah, nor is it assignable to business done by plaintiff within the State of Utah.

ARGUMENT

As shown by the foregoing statement of errors it is the contention of plaintiff, first, that it is specifically exempt from the provisions of the Corporation Franchise Tax Act (Chapter 13, Title 80, Revised Statutes of Utah, 1933), and, accordingly, no deficiency could be assessed against it pursuant to said Act; and, second, that if it is not so exempt and said Act applies to plaintiff, nevertheless the said deficiency assessment is erroneous for the reason that it is based upon the inclusion in plaintiff's taxable net income of items of gross income which do not, under the provisions of said Act, consituate taxable net income. These points will be argued seriatim.

Section 80-13-5, Revised Statutes of Utah, 1933, exempts certain corporations from the provisions of said Franchise Tax Act. Subsection 16 of said section provides as follows:

> "Corporations whose sole business consists of holding the stock of other corporations for the purpose of

controlling the management of affairs of such other corporations, if such other corporations make returns under this Chapter."

In other words, corporations of the type referred to in said sub-section 16 are exempt from the provisions of the Franchise Tax Act.

Heretofore, however, the Commission has held that plaintiff did not come within the provisions of said exempting sub-section for two reasons; first, because during the period in question, plaintiff's sole business did not consist of holding the stock of Idaho Bank and Trust Company and Commercial Security Bank for the purpose of controlling the management of the affairs of such corporations, and, second, the plaintiff was authorized by its Articles of Incorporation to do more than simply hold the stock of other corporations for the purpose of controlling the management of the affairs of the same. This position of the Commission, however, is in direct conflict with the holding of this court in the case of *First Security Corporation of Ogden vs. State Tax Commission, 91 Utah 101, 63 Pac. (2) 1062,* wherein no importance was attached by this Court to the fact that the corporation claiming exemption under the sub-section was in fact authorized by its Articles of Incorporation to do more, and in fact did more, than hold stock in other corporations for the purpose of controlling the management thereof.

In that case this court had before it for determination the question of whether the First Security Corporation was exempt from the provisions of said Act by virtue of said subsection 16. This court held the First Security Corporation to be such a corporation as was referred to by said subsection,

and, accordingly, exempt from the provisions of the Act. Plaintiff submits that it is the same type of corporation as the facts in the First Security Corporation case disclosed the First Security Corporation to be, and that its operations are substantially similar, and that as this court held the First Security Corporation exempt from the Act, so must plaintiff likewise be held to be exempt.

The facts in the First Security Corporation case were stipulated. It appeared that the First Security Corporation, (like plaintiff), was a foreign corporation organized primarily (not solely) for the purpose of acquiring by stock ownership the control of banking and other corporations, and that it was qualified as a foreign corporation to do business in the State of Utah. It bought, held and sold stocks of a corporation other than one of its subsidiaries, namely, Amalgamated Sugar Company. (This was similar to the action of plaint -iff in buying, holding and selling stocks in Ohio Oil Company and Socony-Vacuum Oil Company). Like plaintiff, it held stock holders' meetings in Utah at which reports were presented and directors elected, and held Directors' meetings in Utah, at which matters connected with the control and management of the affairs of its subsidiaries were considered. And, finally, it was shown that by its charter it, like plaintiff, had very broad powers, and was not limited to holding stock in other corporations for the purpose of controlling the same. This Court, upon those facts, held the First Security Corporation exempt from the provisions of the Corporation Franchise Tax Act. By the same token, we submit, plaintiff likewise should be held exempt.

The Commission, however, will undoubtedly argue, as

it has heretofore, that this court, in exempting the First Security Corporation, did not consider the fact that by its charter it had broad powers, and that it was not a corporation whose *sole* business consisted in holding stock in other corporations for the purpose of controlling the same. In other words, the Commission will undoubtedly argue that if the Court had properly considered all the facts presented to it which bore upon the question presented to the Court, this court would not, in that event, have held the First Security Corporation exempt. We submit that such argument, if made, is nothing but gratuitous insult to the Court. The facts presented to the Court showed the broad powers of the First Security Corporation, and that it in fact was not a corporation whose *sole* business consisted in managing, by stock ownership, the affairs of other corporations. The question presented was whether, under all the facts, the corporation came within the exempting subsection. To now suggest that this Court deliberately ignored certain facts bearing upon the question to be decided, to which facts the attention of the Court had been expressly directed, is but to suggest a laxity upon the part of the Court which is unwarranted.

However, if it should be determined that this plaintiff is not exempt from the provisions of the Act, as was the First Security Corporation, despite the fact that the facts with respect to it are substantially identical with the facts relating to plaintiff, nevertheless, plaintiff submits the assessment is erroneous for the reason that it is based upon the inclusion in plaintiff's next taxable income of gross income which cannot under the provisions of the Act, be considered as taxable net income, namely, income derived by plaintiff from business not done by it within the State of Utah.

Section 80-13-21, Revised Statutes of Utah, 1933, entitled "Rules for Determining Net Income Allocated to this State" provides as follows:

"The portion of net income assignable to business done within this State, and which shall be the basis and measure of the tax imposed by this Chapter, may be determined by an allocation upon the basis of the following rules:

(1) Rents, interest and dividends derived from business done outside this state less related expenses shall not be allocated to this state.

(2) Gains from the sale or exchange of capital assets consisting of real or tangible personal property situated outside this state less losses from the sale or exchange of such assets situated outside this state shall not be allocated to this state.

(3) Rents, interest and dividends derived from business done in this state less related expenses shall be allocated to this state.

(4) Gains from the sale or exchange of capital assets consisting of real or tangible personal property situated within this state less losses from the sale or exchange of such assets situated in this state shall be allocated to this state.

(5) If the bank or other corporation carries on no business outside this state, the whole of the remainder of net income may be allocated to this state.

(6) If the bank or other corporation carries on any business outside this state, the said remainder may be divided into three equal parts:

(a) Of one third, such portion shall be attributed to business carried on within this state as shall be found

by multiplying said third by a fraction whose numerator is the value of the corporation's tangible property situated within this state and whose denominator is the value of all the corporation's tangible property wherever situated.

(b) Of another third, such portion shall be attributed to business carried on within this state as shall be found by multiplying said third by a fraction whose numerator is the total amount expended by the corporation for wages, salaries, commissions or other compensation to its employees and assignable to this state and whose denominator is the total expenditure of the corporation for wages, salaries, commissions or other compensation to all of its employees.

(c) Of the remaining third, such portion shall be attributed to business carried on within this state as shall be found by multiplying said third by a fraction whose numerator is the amount of the corporation's gross receipts from business assignable to this state and whose denominator is the amount of the corporation's gross receipts from all its business.

(d) The amount assignable to this state of expenditures of the corporation for wages, salaries, commissions or other compensation to its employees shall be such expenditures for the taxable year as represents the compensation of employees not chiefly situated at, connected with or sent out from, premises for the transaction of business owned or rented by the corporation outside this state.

(e) The amount of the corporation's gross receipts from business assignable to this state shall be the amount of its gross receipts for the taxable year from

(1st) Sales, except those negotiated or effected in behalf of the corporation by agents or a-

gencies chiefly situated at, connected with or sent out from premises for the transaction of business owned or rented by the corporation outside this state, and sales otherwise determined by the tax commission to be attributable to the business conducted on such premises,

(2nd) Rentals or royalties from property situated, or from the use of patents, within this state.

(f) The value of the corporation's tangible property for the purpose of this section shall be the average value of such property during the taxable year.

(7) In the allocation of net income, gain or loss shall be recognized and shall be computed on the same basis and in the same manner as is provided in this chapter for the determination of net income.

(8) If in the judgment of the tax commission the application of the foregoing rules does not allocate to this state the proportion of net income fairly and equitably attributable to this state, it may with such information as it may be able to obtain make such allociation as is fairly calculated to assign to this state the portion of net income reasonably attributable to the business done within this state and to avoid subjecting the taxpayer to double taxation."

As heretofore pointed out, plaintiff, during the period in question, received income by way of dividends on stock owned by it in Idaho Bank and Trust Company in the sum of $6,016.60, in Ohio Oil Company in the sum of $200.00, and in Socony Vacuum Oil Company in the sum of $125.00. Likewise it had gains from the sale of stock in Ohio Oil Company in the sum of $299.40, and from the sale of stock in Socony Vacuum Oil Company in the sum of $4,424.30. As there is

no suggestion by the Commission that application of subsections (1), (2), (3) and (4) above quoted would not allocate to this state the proportion of net income fairly and equitably attributable thereto (referring to subsection (8)), allocation of plaintiff's net income should be made pursuant to said subsections (1), (2), (3) and (4). Plaintiff submits that such dividends and such gains are within the provisions of the subsections, and are not, therefore, allocable to income assignable to business done within the State. In this regard we will first consider the dividends.

It will be noted that the language of the statute is that "dividends derived by business done outside this state less related expenses shall not be allocated to this state". The question to be determined, accordingly, is whether dividends received by plaintiff on its several stocks were derived by it from "business done outside this state" or from "business done in this state". In considering this question an important factor must be borne in mind. It is that plaintiff was a non-resident of the State of Utah, and was doing business in Utah solely by virtue of its compliance with the laws of Utah relative to foreign corporations desiring to do business therein. The state of its domicile was the state of its incorporation, namely, Nevada. The fact that it was doing business in states other than that of Nevada (and it is not denied that it was doing business in other states, including Utah) does not alter the fact that it was domiciled in Nevada, and a non-resident insofar as states other than Nevada are concerned. *Booth v. Weigand, 28 Utah 372, 79 Pac. 570; Wilson v. Triumph Cons. Min. Co. 19 Utah 66; 56 Pac. 300.* This is not a case of a state endeavoring to tax the entire income of one of its citizens from whatever source it may be derived. Such, we con-

cede, might be done if the taxing statute so provided. But here the state of Utah is endeavoring to base a tax upon and measure the same by the income of one who is not one of its citizens. In so doing it is limited to a consideration of income derived solely from business done within its borders, as it cannot use as the basis of the tax income from business done without the state. *California Packing Corporation v. State Tax Commission, 97 Utah 367, 93 Pac. (2) 463.* It is important, accordingly, to determine whether the receipt of dividends by plaintiff on stock of corporations which did no business within the state of Utah constitutes income derived by plaintiff from business done by it within such state.

The Supreme Court of the United States early adopted the rule that the situs of intangibles for taxation purposes is the domicile of the owner. *Blodgett v. Silberman, 277 U. S. 1, 48 S. Ct. 410, 72 L. Ed. 749; Baldwin v. Missouri, 281 U. S. 586, 50 S. Ct. 436, 74 L. Ed. 1056.* Subsequently such court modified such rule somewhat in the case of *Wheeling Steel Corporation v. Fox, 298 U. S. 193, 56 S. Ct. 773, 80 L. Ed. 1143,* by holding that intangibles can acquire a business situs apart from the residence of the owner so as to be there taxable. Still more recent decisions have tended back to the original domicile theory of taxation of intangibles. *Newark Fire Ins. v. Board of Tax Appeals, 59 S. Ct. 918, 83 L. Ed. 1312, 307 U. S. 313; Curry v. McCanless, 59 S. Ct. 900; 83 L. Ed.* 1339, 307 *U. S.* 357. *And so if this case involved the* question of the power of the state to tax the intangibles themselves it might become necessary for this court to decide which theory it would follow. But that question is not here involved, nor is it necessary for this court to determine whether the stocks themselves acquired such a situs within

the State of Utah as to permit such state to tax them. We are here concerned with quite a different matter, namely, the question of the income (dividends) received from the stock, as distinguished from the stock itself. This question cannot be answered simply by a determination of the situs of the stock itself for the purpose of taxation, but depends upon entirely different considerations. In this connection we do not desire to be taken as conceding that the stock itself had acquired a situs in Utah sufficient to justify a tax thereon. The record is entirely devoid of any showing relative thereto other than that the stock was kept in Utah as a matter of convenience to the owner, and even those courts which have permitted the taxation of intangibles in states other than that of the domicile of the owner on the theory that such intangibles have acquired a "business situs" separate and apart from that of the owner, require definite evidence that the intangibles were integral parts of the business conducted. As pointed out by the Supreme Court of the United States in the case of *Newark Fire Ins. v. Board of Tax Appeals, supra,*

> "To overcome the presumption of domiciliary location, the proof of business situs must definitely connect the intangibles as an integral part of the local activity. The facts presented by this record fall far short of this requirement."

And by the same court in the case of *New York ex rel. Cohn v. Graves, 81 L. Ed. 666, 300 U. S. 308,* wherein it was contended by the resident tax payer that certain bonds (which were physically located outside the taxing state) had attained a "business situs" separate and apart from that of his residence:

"Appellant also argues that the interest from the bonds is immune from taxation by New York because they have acquired a business situs in New Jersey within the doctrine of New Orleans v. Stempel, * * * *. This contention, if pertinent to the present case, is not supported by the record. The stipulation of facts discloses only that the bonds and mortgages were located in New Jersey. * * * * The burden rested upon the tax payer to present further facts which would establish a "business situs"."

Similarly interesting is the discussion of the Supreme Court of Oklahoma on this point in the case of *Chestnut Securities Co. v. Oklahoma Tax Commission et al., 48 Pac. (2) 817.* Chestnut Securities Corporation was a Delaware Corporation, having been granted its charter December 14, 1931. On December 28, 1931, it was licensed to do business in Oklahoma. All of its stockholders and directors lived in Tulsa, Oklahoma; all of its business was transacted from its Tulsa office; all of its directors meetings were held in Tulsa; all of its properties were controlled from Tulsa (although certain of its intangibles were physically absent from Oklahoma); and it was also shown that the Company did no business anywhere except in Oklahoma. In considering the question as to whether the intangibles which were physically absent from Oklahoma had acquired a business situs there, the Court said:

"The corporation is a legal entity separate and distinct from the directors and officers. The residence of the latter cannot affect the domicile of the former, and we do not consider the residence of the directors a determining factor herein. Control of the intangible property is a factor to be considered, but such control must be so evercised that the intangible property is actually used or employed by the non-resident corporation in its business transacted in this state. There is

evidence that these stocks, bonds, etc., were never used in the business of plaintiff transacted in this state. It is true that the evidence also discloses that the plaintiff did not transact business at any other place, but it is not inconceivable that at the time the plaintiff received its charter from the state of Delaware, or at least before it was licensed to do business in this state, it invested a part of its capital stock in the intangible properties which are sought to be taxed here and held them thereafter as an investment. There is no evidence that plaintiff purchased and held these properties in foreign states for the purpose of evading the tax laws of this state, and we cannot presume that it did so."

In the present case, plaintiff contends the evidence failed to disclose that the stock had acquired a business situs in Utah. If such was the case the only situs it had was a domiciliary situs in the state of Nevada. As neither the stock itself, nor the enterprise represented by the stock, had a situs in the state of Utah, under the decision of this court in the case of *California Packing Corporation v. State Tax Commission, supra,* the income therefrom was not taxable. However, if we care to assume that the stock itself did have a business situs within the state of Utah, nevertheless the income therefrom is not taxable by Utah, nor can it be used as a basis for a determination of the tax under the Franchise Tax Act, for the reason that the income on the stock (dividends), as distinguished from the stock itself, was not derived from business done by plaintiff within the State of Utah. The act says that "dividends derived from business done outside this state * * * * shall not be allocated to this state". The dividends which this plaintiff received from Idaho Bank and Trust Company were from business done by that company in Idaho. No business, which resulted in the payment of dividends by that com-

pany to plaintiff, was done in Utah. The dividends were earned in Idaho, and payment thereof made in Idaho. The fact that they were received by plaintiff in Utah cannot be construed as meaning that they were received from business done in Utah. Plaintiff might have requested that the checks be mailed to it in any other state, and such a request and subsequent compliance therewith by the bank, could not constitute doing business in the state to which the checks were mailed.

It seems to us that an analysis of the statute can result in no other conclusion than that to which we have arrived, namely, that the receipt of dividends in the State of Utah on stock physically held therein by a non-resident, which stock is in a corporation foreign to the State of Utah and which does no business within the State of Utah, does not constitute income derived from business done in the State of Utah, and that authority to support such conclusion should be unnecessary. It may be lack of necessity for such authority accounts for the dearth thereof, as plaintiff has been unable to find but a single case directly in point. Such case is *Stanley Works v. Hackett, Tax Commissioner, 190 Atl. 743 (Conn.)*. Stanley Works was a Connecticut corporation, and it, in the year 1935, in addition to other business done by it, held stock in three Canadian corporations, being the sole owner of all of the stock of such corporations. Such corporations were, however, under the active management of managers resident in Canada, and did no business whatever outside the Dominion of Canada. Stanley Works received the sum of $720,975 in dividends on its stock holding in such corporations, showing the same in its return to the state of Connecticut, but not including the same in its computation of the

amount of the franchise tax due the state of Connecticut. The tax commissioner overruled the Company's claim that such amount should not be included in the computation of the tax and imposed an additional tax of $14,168,99 on account of this item. We quote the following from the opinion of the Oklahoma court in that case:

> "We are not here concerned with the bare question whether in measuring a tax imposed upon a corporation for the privilege of doing busines sin a state dividends received upon the stock of other corporations may be included with income it receives from other sources. See McCoach v. Minehill & S. H. R. Co., 228, U. S. 295, 308, 33 S. Ct. 419, 57 L. Ed. 842. The question before us is whether, in working out the scheme of the statute for the allocation of income within and without the state, dividends upon the stock of the Canadian corporations fall within one class or the other. The specific provision of the statute determinative of the present case is as follows: 'Interest,dividends, royalties and gains from sales of intangible assets, less related expenses, when received by a company having its principal place of business within the state, shall be allocated to the state and, when received by a company having its principal place of business without the state, shall be allocated without the state; provided, when it can be clearly established that such income is received in connection with business within the state, such income shall be allocated to the state without regard to the location of the principal place of business of the taxpayer, and a similar rule shall apply to such income received in connection with business without the state.' Section 420c(1).
>
> The method of allocation provided is applied to net income. As under the provision concerning deductions dividends upon the stock of domestic corporations are in in general to be deducted in the determination of the net

income, it follows that the word 'dividends' as used in the quotation above can only refer to dividends upon the stock of the small class of corporations of this country which do not pay a federal income tax or dividends received upon stock of foreign corporations. The state contends that the phrase 'in connection with business within the state' and the corresponding phrase with reference to 'business without the state' refer only to the business done by the corporation itself within or without the state, that the business done by the Canadian corporations cannot properly be regarded as business done by the plaintiff and that therefore the provision is not applicable. While for many purposes the law might not regard the plaintiff as doing business in Canada by reason of the ownership of all the stock in the Canadian corporations, in our approach to tax legislation we may properly view it from the standpoint of substance, and not of form (Cardozo, J., People ex rel. Alpha Portland Cement Co. v. Knapp, 230 N. Y. 48, 57, 129 N. E. 202); and, if we do, we cannot avoid the conclusion that the plaintiff 'made use of the activities of these subsidiary corporations as essential parts of its business' (National Leather Co. v. Commonwealth, 256 Mass. 419, 423, 152 N. E. 916, 917); and that it 'did, in a very real and practical sense, employ these stocks as an instrumentality in carrying on its business' (National Leather Co. v. Massachusetts, 277 U. S. 413, 423, 48 S Ct. 534, 535, 536, 72 L. Ed. 935); so that the business of the Canadian corporations might be regarded as its business. Moreover, the contention of the state would necessarily exclude all 'dividends' received by the plaintiff from the operation of the provision in question, because they would only represent ownership of stock of corporations other than the plaintiff. This would require that the words 'such income' be related to the other three items mentioned at the beginning of the provision to the exclusion of 'dividends'; and such grammatical construction has no warrant in the terms of the

statute. In fact, the use of the broad words 'in connection with business' has significance, for had the narrower construction contended for by the state been intended, it would have been natural for the Legislature to use a phrase with a more restricted meaning. The intent of the statute as regards 'dividends' within the scope of this provision evidently was a substitute for the complicated provisions of the federal act designed to afford protection against double taxation as regards dividends not deductible in determining net income, a simpler provision applicable alike to them and to the other types of income delt with in this portion of the law. As in this case the dividends in question were all earned upon business done in the Dominion of Canada, they should be allocated without the state."

While, as heretofore pointed out, we have been unable to find but the single case wherein the courts have found it necessary to advise the taxing authorities of a state that they cannot tax the income of a foreign corporation received as dividends upon stock owned by it in a second foreign corporation, the courts have, on numerous occasions, held that the owning or holding of stocks in domestic corporations does not constitute "doing" or "transacting" business within the states of the domestic corporations domicile, even though the stock ownership is sufficient to control the domestic corporations, and that the purchase of stock does not constitute doing or transacting business. *Crockin v. Boston Store of Ft. Myers, 188 So. 853 (Fla); State ex rel City of St. Louis v. Public Service Commission of Missouri, 73 S. W. (2) 393; United States Rubber Company v. Query, 19 F. Supp. 191; Mannington v. Hocking Valley Ry Co., 183 Fed. 133; State v. Humble Oil & Refining Co., 263 S. W. 319 (Tex.).* In other words even though Idaho Bank and Trust Company had been a

Utah corporation, the income received by plaintiff as dividends on stock held therein would not be taxable in Utah under the present Utah statute, because, the statute bases the tax only on income received from "business done in this state", and the holding of stock does not constitute "doing business". Since the holding of stock by plaintiff in a Utah corporation would not constitute the doing of business by plaintiff in Utah, the receipt of dividends on such stock holdings could not be construed as income from business done in this state. Thus considered it is inconceivable upon what theory the holding of stock by plaintiff in a foreign corporation could be construed as the doing of business by plaintiff in Utah, so as to constitute dividends received by it on such stock holdings as income received from "business done in this state".

We have so far limited our discussion to a consideration of the dividends received by plaintiff upon stock held by it in Idaho Bank and Trust Company, but what has been said as to those dividends applies with even greater force to the dividends received upon stock held in Socony Vacuum Oil Company and Ohio Oil Company, as plaintiff was but another stockholder insofar as those companies were concerned, while it was the principal stockholder of Idaho Bank and Trust Company. Holding or owning stock by a foreign corporation in another corporation does not constitute "doing business" in a state other than that of the foreign corporation's domicile, (cases cited *supra*), and, accordingly, dividends received by plaintiff on stock owned by it in other corporations are not dividends from "business done in this state".

Consideration of plaintiff's gains from the sale of stock

of Socony Vacuum Oil Company and Ohio Oil Company requires a somewhat different approach than that involved in the consideration of the dividends received by plaintiff. As a premise to this portion of our argument, we submit the proposition that if the gain is to be allocated to Utah for the purpose of determining the amount of plaintiff's franchise tax the same must be allocated pursuant to Section 80-13-21, Revised Statutes of Utah, 1933, heretofore set out in full herein. In other words, since we are dealing with the problem of determining the amount plaintiff owes the State of Utah for the privilege of doing business therein for a certain year, and since the legislature has seen fit to provide certain rules for the determination thereof, such determination must be in accord with such rules as so fixed by the legislature. We do not suggest that the legislature could not have fixed other rules, or more inclusive rules, but that the rules fixed by the legislature, whatever they may be, are exclusive of any other method of determination.

It will be noted that included in the rules for determining net income allocated to this state as fixed by the legislature are two rules and no others dealing with gains from the sales or exchange of capital assets, which rules are set out in subsections (2) and (4) of Section 80-13-21. (We are, in this connection, excluding consideration of subsection (8), because the Tax Commission has never intimated that such subsection had any application here.) Subsection (2) provides that "gains from the sale or exchange of capital assets consisting of *real or tangible* property situate outside this state * * * shall not be allocated to this state," while subsection (4) provides that "gains from the sale or exchange of capital assets consisting of *real or tangible property* situated within

this stat * * * shall be allocated to this state". (italics supplied) Those two subsections deal exclusively with real or tangible property, and do not purport to refer in any wise to *intangible* property. The legislature has, therefore, failed to provide for allocation of gains from the sale or exchange of intangible property, and, having so failed, the Commission has no authority to make any allocation whatever of the gains from the sale or exchange of intangible property, and a consideration thereof has no place in the determination of plaintiff's franchise tax. As shares of stock in corporations are in tangible property — *Gallatin County Farmers' Alliance v. Flannery, 197 Pac. 996, and cases therein cited* — it follows that plaintiff's gain from the sale of its stock holdings in Socony Vacuum Oil Company and Ohio Oil Company constituted gains from the sale of intangible property, and the Tax Commission was without authority to allocate the same. Again we desire to point out that we are not urging that the legislature could not have provided for allocation of gains from the sale of intangibles, the same as it provided for allocation of dividends received therefrom, but it has not so provided and the Commission is bound by what the legislature has done in this regard, and not by what it could have done.

It is not, however, necessary fo rplaintiff to rest upon the failure of the legislature to allocate these gains, because, had subsection (2) and (4) included gains from the sale or exchange of intangibles as well as tangibles, the gains received from the sale by plaintiff from the sale of these stocks would have been allocated outside the state under subsection (2), for the reason that they are gains from the sale of property situate outside the state of Utah. This because, as they

are intangibles, the presumption is that their situs is the domicile of plaintiff, namely, Nevada, and there is no sufficient showing that they had attained a business situs in Utah separate and apart from their domiciliary situs.

CONCLUSION

Accordingly it is submitted ~~It is not, however, necessary for plaintiff to rest upon~~ that the decision of the Tax Commission in assessing a deficiency tax against plaintiff for the privilege of doing business in Utah during the year 1935, is erroneous, first, because it was assessed pursuant to Chapter 13, Title 80, Revised Statutes of Utah, 1933, and such Chapter has, by virtue of Section 80-13-5 (16) no application to plaintiff, second, because it is based upon the inclusion in plaintiff's net taxable income of dividends received by plaintiff on stock owned by it, which dividends were not derived from business done in this state, and, accordingly, were not allocable to Utah, and, third, because it is based upon the inclusion in plaintiff's net taxable income of gains to plaintiff from the sale of intangible property, and gain from the sale of intangibles are not, under the provisions of 80-13-21, Revised Statutes of Utah, 1933, allocable to Utah.

Respectfully submitted,

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